Internal Revenue Service

memorandum

CC:TL-N-2855-90
Br4:RJFitzpatrick

date: APR 19 1990

to: District Counsel, San Diego CC:SD
Attn: Mr. Lowrance

from: Assistant Chief Counsel (Tax Litigation) CC:TL

subject: [redacted]

This responds to your request for Tax Litigation Advice on the settlement of a claim for attorney fees in the above-entitled action. Based upon the inaction of District Counsel, we concur with your recommendation that this case be settled for $[redacted].

Petitioners filed their petition with the Tax Court on [redacted]. Amendments made to I.R.C. § 7430 by the Tax Reform Act of 1986 (TRA 86), Pub. L. 99-514, 100 Stat. 2085, 2752-2753, apply to proceedings commenced after December 31, 1985. Amendments made to I.R.C. § 7430 by the Technical and Miscellaneous Revenue Act of 1988 (TAMRA), Pub. L. 100-647, 102 Stat. 3342, 3743, apply to proceedings commenced after November 10, 1988. Accordingly, the amendments to I.R.C. § 7430 by TRA 1986 apply to this matter, but the TAMRA amendments do not.

I.R.C. § 7430(a) provides for the award of reasonable litigation costs to a taxpayer who is the "prevailing party" in a proceeding in the Tax Court. To be the "prevailing party" a taxpayer must:

(1) Establish that the "position of the United States" (I.R.C. § 7430(c)(4) [now I.R.C. § 7430(c)(7)]) in the civil proceeding was not substantially justified (I.R.C. § 7430(c)(2)(A)(i);

(2) substantially prevail with respect to the amount in controversy, or with respect to the most significant issue of set of issues presented (I.R.C. § 7430(c)(2)(A)(ii)); and

(3) have a net worth which did not exceed $2 million at the time the case was initiated (see I.R.C. § 7430(c)(2)(A)(iii)).

The Tax Court has interpreted the definition of the term "position of the United States" contained in I.R.C. § 7430(c)(4) as including only those actions or inactions occurring at or after the point at which District Counsel becomes involved

in the proceedings. Ganter v. Commissioner, 92 T.C. 192, 194 (1989); Egan v. Commissioner, 91 T.C. 705, 712 (1988); Sher v. Commissioner, 89 T.C. 79, 86 . (1987), affd. 861 F.2d 131 (5th Cir. 1988). The circuit courts of appeal are split on the issue of whether the pre-litigation position of the United States should be examined.1/

It is clear that petitioners mailed the 872-Ts to the Service on or about [redacted] (received by the Service on [redacted]. A notice of deficiency for the [redacted] year was issued prior to the 90 day expiration date of receipt of the 872-T. A notice of deficiency for [redacted] was not issued until [redacted] well after the expiration of the 90 days allowed for issuance of a notice.

Prior to filing with the Tax Court, petitioners raised the statute of limitations with District Counsel, Manhattan. District Counsel advised petitioner that petitioners would have to file with the Tax Court and that nothing could be done until after a petition was filed. On [redacted], petitioners filed with the Tax Court. Despite the fact that petitioners alleged that they mailed an 872-T to the Service for [redacted], District Counsel on [redacted] denied that the Service received an 872-T and alleged that the notice of deficiency was issued prior to the expiration of the statute of limitations. On [redacted] District Counsel filed a Motion for Entry of Order that the undenied allegations in answer be seemed admitted (that the Service had not received the 872-T for the [redacted] tax year). On [redacted], the Tax Court denied the Service's motion. The [redacted] case was placed on the [redacted] calendar in [redacted], California. The only issue for litigation was the statute of limitations issue.

1/ The Eighth, Tenth, Eleventh, and District of Columbia Circuits have approved the position of the Service and the Tax Court. Berks v. United States, 860 F.2d 841 (8th Cir. 1988); Wickert v. Commissioner, 842 F.2d 1005, 1008 (8th Cir. 1988); Ewing and Thomas, P.A. v. Heye, 803 F.2d 613, 615-616 (11th Cir. 1986); Baker v. Commissioner, 787 F.2d 637, 641 (D.C. Cir. 1986); United States v. Balanced Financial Management, Inc., 769 F.2d 1440, 1450 (10th Cir. 1985); Ashburn v. United States, 740 F.2d 843, 848 (11th Cir. 1984). The First, Fifth, Sixth, and Ninth Circuits have permitted both pre-litigation and litigation positions to be examined. Comer Family Trust v. Commissioner, 856 F.2d 775, 780 (6th Cir. 1988); Silwa v. Commissioner, 839 F.2d 602, 606 (9th Cir. 1988); Powell v. Commissioner, 791 F.2d 385, 388-292 (5th Cir. 1986); Kaufman v. Egger, 758 F.2d 1, 4 (1st Cir. 1985).

Sec. 1551(e) of the Tax Reform Act of 1986, supra, amended I.R.C. § 7430(c) by adding a new paragraph (4) defining "position of the United States" as follows:

(4) POSITION OF UNITED STATES.-The term "position of the United States" includes-

(A) the position taken by the United States in the civil proceeding, and

(B) any administrative action or inaction by the District Counsel of the Internal Revenue Service (and all subsequent administrative administrative action or inaction) upon which such proceeding is based.

The case was transferred to San Diego on [redacted]. Shortly thereafter, during preparation for trial, your office determined that an 872-T had been received by the Service and therefore promptly conceded this issue. It is clear that petitioners substantially prevailed with respect to the most significant issue in this case and from the facts provided our office, it does not appear that petitioners' net worth exceeded $[redacted] at the time the petition was filed in this case.

We agree with your office that under the facts in this case, it is likely that the both Tax Court and Ninth Circuit would find that the "position of the United States" was unreasonable due to the inaction of District Counsel in not determining whether the 872-T was sent to the Service in a reasonable manner and within a reasonable amount of time. There is no need to even consider the administrative position prior to District Counsel's involvement, since we feel this case should be conceded on the basis of District Counsels inaction. Overall, we concur with your office's recommendation that attorney fees be paid in the amount requested by petitioners. Without repeating your lengthy discussion of the administrative activities prior to District Counsel involvement, we concur with your office's view that the Ninth Circuit (the venue of an appeal in this case) would pose even more significant litigation hazards than even the Tax Court. We therefore authorize your concession of the attorney fees request in this case.

MARLENE GROSS
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(Tax Litigation)

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cc: Regional Counsel CC:W

Attachments:
Exhibits Returned (6)